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BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
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IN THE MATTER OF THE APPLICATION OF
PAYSON WATER CO., INC. AN ARIZONA
CORPORATION, FOR A DETERMINATION OF
THE FAIR VALUE OF ITS UTILITY PLANT
AND PROPERTY AND FOR INCREASES IN ITS
WATER RATES AND CHARGES FOR UTILITY
SERVICE BASED THEREON.

DOCKET NO. W-03514A-13-0111

ORIGINAL

IN THE MATTER OF THE APPLICATION OF
PAYSON WATER CO., INC. FOR AUTHORITY
TO ISSUE EVIDENCE OF INDEBTEDNESS IN
AN AMOUNT NOT TO EXCEED \$1,238,000 IN
CONNECTION WITH INFRASTRUCTURE
IMPROVEMENTS TO THE UTILITY SYSTEM;
AND ENCUMBER REAL PROPERTY AND
PLANT AS SECURITY FOR SUCH
INDEBTEDNESS.

DOCKET NO. W-03514A-13-0142

STAFF'S REPLY BRIEF

The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") files its reply brief to address matters raised in the parties' initial briefs.

I. NOTICE WAS PROPER IN THE PHASE 1 PROCEEDING**A. Introduction.**

Phase 1 of this proceeding was held on September 25, 2013. A number of public commenters took issue with the notice that was provided. During the Phase 1 public comment session, Administrative Law Judge ("ALJ") Nodes explained:

With regard to the notice, and I just want to let you know that the actual hearing on the rate implication involving all the systems' permanent rates is not going to occur until January. So, and I think that that is included in the notice. This is just an interim Phase 1 consideration of the financing application that's applicable only to the Mesa Del Caballo proposed pipeline. And that's why we are here today, because they are trying to get financing through WIFA, which has a more immediate deadline as far as the financing. But it has nothing to do with the permanent rates and it has nothing to do with people outside Mesa Del Caballo.¹

¹ Tr. 22:20-23:7.

1 Despite this explanation, complaints regarding the notice persist. Intervenor Bremer,
2 Sheppard, Nee and Reidhead make various arguments in their briefs regarding notice, and their
3 inability to intervene in the Phase 1 proceeding. It should be noted that none of these intervenors live
4 or own property in Mesa Del Caballo ("MDC") and are not directly affected by the Commission's
5 decision in Phase 1. In any event, Decision No. 74175 is final and non-appealable.

6 However, because intervenors have raised these matters again, Staff hereby responds to the
7 alleged notice issues as follows. A.R.S. § 40-243 gives the Commission the authority to adopt rules
8 of practice and procedure. Arizona Administrative Code ("A.A.C.") R14-2-105 requires that all
9 public service corporations give notice to customers of their rate applications, and that the form and
10 manner of notice shall be as the Commission may direct by procedural order. The procedural order
11 dated September 10, 2013, not only required notice to be mailed, but to also be published in a
12 newspaper of general circulation. Notice was to be provided to MDC customers by September 20,
13 2013, and to all other customers by October 15, 2013. The Company filed an affidavit attesting to the
14 mailing and publication of notice as was required by the procedural order.

15 Further, the applicable rule for Commission proceedings is A.A.C. R14-3-109 which states
16 that 10 days notice is to be given prior to a hearing "unless otherwise provided by law or as ordered
17 by the Commission." As was discussed in Decision No. 74175, the Water Infrastructure Financing
18 Authority ("WIFA") deadline for financing approval by the Commission necessitated the scheduling
19 of an expedited hearing in order for the first phase of the pipeline project to be completed by summer
20 2014. This was done to enable the Company to deliver water directly from the Town of Payson, and
21 to avoid the expensive water hauling charges that had been assessed to MDC customers in prior
22 years.

23 Ms. Nee and Mr. Sheppard assert that the notice was insufficient because it was mailed in a
24 plain white envelope with a return address, which was not the address of the Company.² Ms. Nee
25 states she almost threw it away as junk mail.³ Mr. Sheppard also argues that there is no way of
26 knowing whether all affected by the notice actually received notice because they may have thrown it

27 ² Tr. at 528: 15-25; 529: 1-5.

28 ³ *Id.*

1 away. He asks that the rate application be dismissed, and that the Company be ordered to re-file its
2 application.⁴

3 The general rule is that someone having actual notice is not prejudiced by, and may not
4 complain of, the failure to receive statutory notice.⁵ The Commission's rules do not specify all of the
5 technical attributes, e.g., type of envelope, of the notice mailing. Notwithstanding the plain white
6 envelope and unknown return address, there were 12 people who gave public comment during the
7 Phase 1 proceeding. Of those 12 public commenters, 6 were granted intervention in Phase 2. These
8 individuals obviously received notice.

9 With respect to the argument that people may not have received the mailed notice, or received
10 it but threw it away without reading, Arizona recognizes what is best termed a "mail delivery rule."⁶
11 Under the mail delivery rule, there is a presumption that a "letter properly addressed, stamped and
12 deposited in the United States mail will reach the addressee."⁷ Proof of the fact of mailing will,
13 absent any contrary evidence, establish that delivery occurred. If, however, the addressee denies
14 receipt, the presumption of delivery disappears, but the fact of mailing still has evidentiary force.⁸
15 The denial of receipt creates an issue of fact that the fact finder must resolve to determine if delivery
16 actually occurred.⁹ There was no testimony presented in either Phase 1 or Phase 2 that notice was not
17 received.¹⁰

18 **B. The notice provided in the Phase 1 proceeding does not violate due process.**

19 Ms. Reidhead and Ms. Nee argue that the prescribed notice violated due process because it
20 was not received in time for intervention in the Phase 1 proceeding.¹¹ While not framed in those
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22 ⁴ Sheppard br. at 3.

23 ⁵ *Larabee v. Washington*, 793 S.W.2d 357 (Mo.App.1990); *First National Bank v. Oklahoma Savings*
24 *and Loan Board*, 569 P.2d 993 (Okl.1977).

25 ⁶ *Lee v. State*, 218 Ariz. 235, 237, 182 P.3d 1169, 1171 (2008).

26 ⁷ *Id.*

27 ⁸ *Id.* citing *Andrews v. Blake*, 205 Ariz. 236, 242 ¶ 22 n. 3, 69 P.3d 7, 13 n. 3 (2003).

28 ⁹ *Id.*

¹⁰ Intervenor Ross stated in his closing brief that some customers did not received notice. Ross br. at
3.

¹¹ Reidhead br at 1-3; Nee br. at 2-3.

1 terms, Mr. Bremer makes a similar argument.¹² Mr. Bremer, Ms. Nee and Ms. Reidhead appeared at
2 the Phase 1 hearing to give public comment. At no time did they request to intervene. Thus, these
3 intervenors cannot demonstrate that they have standing to assert a due process violation associated
4 with the Phase 1 proceeding. Absent a showing that a constitutionally protected interest is affected,
5 the protections embodied in due process do not attach.

6 The Phase 1 proceeding addressed the Company's expedited request for Commission
7 approval of a \$275,000 WIFA loan to finance a portion of the planned interconnection to the Cragin
8 Pipeline. The project enables the Company to interconnect the MDC system to the Town of Payson
9 so that water could be obtained directly from the Town rather than having to haul water by truck
10 during periods of water shortages. Because this Phase 1 proceeding affected only MDC customers,
11 the Company was ordered to provide notice to those customers at an earlier date. Mr. Bremer, Ms.
12 Reidhead and Ms. Nee are not customers of the MDC system.¹³

13 In an attempt to bolster their claims of a due process violation, Ms. Nee and Ms. Reidhead
14 continue to assert that the rates being set during Phase 2 are a direct result of findings in Phase 1,
15 despite sworn testimony and the express language of Decision No. 74175 to the contrary. The
16 concepts embodied in due process protect against unreasonably arbitrary government actions
17 (substantive due process) and procedurally defective government processes (procedural due
18 process).¹⁴ A threshold requirement to a substantive or procedural due process claim is the plaintiff's
19 showing of a liberty or property interest protected by the Constitution.¹⁵ In order to show a
20 substantive due process violation, the abuse of governmental power must be one that "shocks the
21 conscience."¹⁶

22 ¹² Bremer br. at 3.

23 ¹³ Ms. Reidhead owns vacation property in Deer Creek; Ms. Nee owns vacation property in Meads
24 Ranch; Mr. Bremer owns vacation property in EVP.

24 ¹⁴ See *Sulger v. Ariz. Corp. Comm'n*, 5 Ariz. App. 69, 73, 423 P.2d 145, 149 (1967).

25 ¹⁵ *Aegis of Arizona, L.L.C. v. Town of Marana*, 206 Ariz. 557 (2003) (citing *Wedges/Ledges of California, Inc. v. City of Phoenix*, 24 F.3d 56, 62 (9th Cir.1994)).

26 ¹⁶ See *County of Sacramento v. Lewis*, 523 U.S. 833, 834 (1998); *United Artists Theatre Circuit, Inc. v. Township of Warrington*, 316 F.3d 392, 401 (3rd Cir.2003); *Eller Media Co. v. City of Tucson*, 198 Ariz. 127, ¶ 6, 7 P.3d 136, ¶ 6 (App.2000) (noting that substantive due process "precludes government conduct that shocks the conscience").
27
28

1 Mr. Bremer, Ms. Nee and Ms. Reidhead cannot meet the threshold showing to assert a
2 violation of alleged due process rights concerning an alleged inability to participate in the Phase 1
3 proceeding. Simply stated, there is no protected interest at play. A liberty interest involves
4 restrictions on a person's physical freedom or the ability to engage in one's profession. Intervenor
5 are not MDC customers, and are not subject to the surcharge that was approved. Decision No. 74175
6 by its express language, states that the approved surcharge "shall apply only to customers of the Mesa
7 del Caballo system".¹⁷

8 Ms. Reidhead, Ms. Nee and Mr. Bremer argue that, even if intervention had been requested
9 by them and granted by the Commission, they would not have had enough time to prepare. They cite
10 *Hendricks v. Arizona Dept. of Economic Sec* in support.¹⁸ The reliance on *Hendricks* is misplaced.
11 In *Hendricks*, the Arizona Department of Economic Security ("DES") sought to recoup an
12 overpayment of cash assistance from the plaintiff. The notice provided to the plaintiff was incorrect;
13 it stated that DES was attempting to recover an over issuance of food stamps. Ms. Hendricks was
14 unaware of the incorrect notice and the true nature of the proceeding until she appeared at the
15 hearing. It is against this factual background that the Court of Appeals found that Ms. Hendricks was
16 unable to have a meaningful opportunity to be heard.

17 No such factual background exists here. There were no procedural due process violations
18 because Mr. Bremer, Ms. Nee and Ms. Reidhead were granted intervention in Phase 2 of the
19 proceeding, the rate application hearing that would set rates for their respective communities. Mr.
20 Bremer, Ms. Nee and Ms. Reidhead were allowed to present testimony and cross examine witnesses.

21 Finally, although the Phase 1 notice was appropriate, interim rates may be set without notice
22 and opportunity to be heard.¹⁹ In an emergency situation, intervention could delay the proceedings
23 and negate the very reason behind the granting of interim relief.²⁰ The Commission, in granting the
24 water augmentation surcharge for MDC, had already determined that an emergency existed.²¹ In

25 ¹⁷ Decision No. 74175 at 16.

26 ¹⁸ 229 Ariz. 47, 270 P.3d 874 (2012).

27 ¹⁹ Attorney General Opinion No. 71-17 at 7.

28 ²⁰ *Id.*

²¹ See Decision No. 71902.

1 order to receive WIFA approval and commence construction prior to the summer season when
2 hauling of water occurs, the Company needed interim rate relief.

3 **II. THE PHASE 1 PROCEEDING HAS NO IMPACT ON THE RATES BEING SET IN**
4 **PHASE 2**

5 Intervenor Nee and Reidhead argue that the surcharge established in Phase 1 somehow
6 impacts the rates being set in Phase 2.²² Their argument appears to be a misunderstanding concerning
7 how rates are set, perhaps due to a lack of familiarity with the ratemaking process.

8 The surcharge established in the Phase 1 proceeding is set at a level that would enable the
9 Company to recover the monthly payments of principal, interest and fees, and the debt service reserve
10 required by WIFA (20 percent of the loan).²³ Perhaps there is confusion concerning the WIFA
11 requirement that a company have a certain debt service coverage ratio ("DSC") to qualify for a
12 loan.²⁴ As Mr. Cassidy explained in his testimony, the DSC reflects a company's ability to meet
13 cash flow obligations associated with incurring debt.²⁵ The surcharge will allow the Company to
14 service debt independent of any rates that are set as a result of the Phase 2 proceeding.²⁶ Should there
15 be any shortfall in servicing the debt the Company would be responsible, paying any shortfall with
16 equity.²⁷ And, as has been stated numerous times, the surcharge is only assessed on MDC
17 customers.²⁸

18 **III. RATE CONSOLIDATION IS REASONABLE AND SHOULD BE ADOPTED**

19 Staff supports the Company's proposed consolidation of the rates for its United and C&S
20 systems. Several intervenors oppose rate consolidation, and even suggest that the systems be
21 deconsolidated.²⁹ As a general rule, rates are set on cost of service principles. In cost of service
22 regulation, the regulator determines the revenue requirement, i.e., the "cost of service," that reflects
23

24 ²² Nee br. at 4; Reidhead br. at 3-4.

25 ²³ Decision No. 74175 at 7.

26 ²⁴ *Id.* at 10.

27 ²⁵ Tr. at 659:12-13.

28 ²⁶ Tr. at 661:3-16.

²⁷ Tr. at 110:13-23.

²⁸ *Id.* at 16.

²⁹ Reidhead br. at 15; Nee br. at 9-10.

1 the total amount that must be collected in rates for the utility to recover its costs and earn a reasonable
2 return. The Commission has noted that cost of service studies are simply “tools” for establishing
3 revenue requirement per customer class and that it also considers other factors such as rate stability,
4 fairness, conservation, etc.³⁰

5 Consolidation of the rates would provide several benefits. As Company witness Thomas
6 Bourassa testified, there are economies of scale to be gained by consolidation.³¹ He further
7 explained, “[t]he more customers you share the costs over, the less each individual customer has to
8 pay as a result.”³² He identified other benefits such as revenue stability. Consolidation of rates would
9 also smooth over cost spikes by allowing the systems to share, over time, expenses and investment.³³
10 In response to whether each system could be run as a stand-alone entity, Mr. Bourassa testified that it
11 would probably be more expensive because you would lose the advantage of shared resources.³⁴
12 Staff witness Crystal Brown testified that the Commission favors consolidation for small systems, by
13 weighing the benefits of financial stability that can come from consolidation.³⁵ The prior C&S
14 system customers received a benefit when the rates of the prior systems, Gisela and Triple T, were
15 consolidated. In light of the above, United and C&S systems’ rates should be consolidated.

16 IV. ENGINEERING MATTERS

17 A number of intervenors have questioned the adequacy of the Payson water supply,
18 suggesting that the water shortages for MDC were contrived. Staff engineer Jian Liu concluded that
19 “Payson has very fragile water systems.”³⁶ He notes that the majority of the wells have a very low
20 production capacity and are more than 40 years old.³⁷

22 ³⁰ Decision No. 60172 at 40.

23 ³¹ Tr. at 49:23-25.

24 ³² *Id.*

25 ³³ *Id.*

26 ³⁴ Tr. at 51:3-19.

27 ³⁵ Tr. at 700:9-18.

28 ³⁶ Ex. S-7 at 12 of the Engineering Report. Mr. Liu filed pre-filed testimony but was unable to
participate in the Phase 2 proceeding. His pre-filed testimony was adopted by Engineering Supervisor
Del Smith. Mr. Smith testified during the Phase 2 proceeding.

³⁷ *Id.*

1 Even though Phase 1 was no longer an issue, several intervenors continue to suggest that
2 instead of the TOP-MDC pipeline, more wells should be drilled. Further, several intervenors insist
3 that there is an ample water supply in MDC, despite testimony and Commission findings to the
4 contrary.³⁸ As Staff engineer Del Smith testified, drilling wells can be risky and, if the well is dry, the
5 Company would not be allowed to recoup its costs through rates.³⁹ Mr. Smith further testified that
6 wells drilled in MDC for home use were low producers and would not be adequate to serve a
7 community.⁴⁰ Mr. Smith added that, given the low production of the wells in MDC, the TOP-MDC
8 line is a sure source of supply for MDC.⁴¹ Thus, the intervenors' arguments on these points are not
9 supported by the testimony in the record.

10 **V. THE COMPANY ACCEPTS STAFF'S RECOMMENDATION REGARDING THE**
11 **HAULED WATER COST RECOVERY CAP FOR EAST VERDE PARK**

12 In its closing brief, the Company indicated that it now accepts Staff's recommendation that a
13 cap be placed on the total amount of hauled water cost the Company could recover in any given
14 year.⁴²

15 Mr. Bremer proposed an alternative method that would calculate a threshold amount of water
16 used during the May-September augmentation period, within the capability of local well production,
17 below which an EVP customer would not be assessed a water hauling surcharge.⁴³ Staff witness
18 Crystal Brown testified that it would be difficult to obtain the necessary water user information to
19 determine if water was used within the local capacity of the wells to make such a proposal
20 workable.⁴⁴ Staff believes its recommendation is less complicated and more reasonable and,
21 therefore, should be adopted.

22 ...

23 ...

24 ³⁸ See Decision No. 71902 at 10.

25 ³⁹ Tr. at 603:8-14.

26 ⁴⁰ Tr. at 606:17-21.

27 ⁴¹ Tr. at 615-616.

28 ⁴² Company br. at 17.

⁴³ Tr. at 904:16-24, Ex. TB-5.

⁴⁴ Tr. at 901.

1 **VI. INTERVENORS' ALLEGATIONS OF MISCONDUCT IN THE PROCEEDING**

2 Passions and emotions appear to have run high during this proceeding. The possibility of
3 higher rates may often be a cause for concern for customers. However deeply felt this concern may
4 be, it does not give the intervenors free reign to make unmerited claims of misconduct against the
5 Company, Staff and the ALJ. There is no basis in the record for the intervenors' allegations that Staff
6 and the ALJ conspired with the Company against the interests of the customers of Payson.

7 The universal rule is that government officials have a "presumption of honesty and integrity"
8 which is a "difficult burden of persuasion" to overcome.⁴⁵ The leading treatise describes five types of
9 bias:

10 1) A prejudgment or point of view about a question of law or policy, even if so
11 tenaciously held as to suggest a closed mind, is not, without more, a disqualification.
12 (2) Similarly, a prejudgment about legislative facts that help answer a question of law
13 or policy is not, without more, a disqualification. (3) Advance knowledge of
14 adjudicative facts that are in issue is not alone a disqualification for finding those
15 facts, but a prior commitment may be. (4) A personal bias or personal prejudice, that
16 is an attitude toward a person, as distinguished from an attitude about an issue, is a
disqualification when it is strong enough and when the bias has an unofficial source;
such partiality may be either animosity or favoritism. (5) One who stands to gain or
lose by a decision either way has an interest that may disqualify if the gain or loss to
the decision maker flows fairly directly from her decision.⁴⁶

17
18
19 ⁴⁵ *Withrow v. Larkin*, 421 U.S. 35, 47 (1975)(holding that Wisconsin Board of Medical Examiners
20 where not biased adjudicators despite combination of investigative and adjudicative functions). See
21 also *Martin v. Superior Court*, 135 Ariz. 258, 260 (1983)(holding that "administrative hearing
22 officers in Arizona are also assumed to be fair..."); *Ison v. Western Vegetable Distributors*, 48 Ariz.
23 104, 119 C]ommissioners..."); *Jenners v. Industrial Commission*, 16 Ariz. App. 81 (1971)(holding
24 that "an administrative hearing officer can only be disqualified upon a showing of actual bias, and not
25 even then if ... no other hearing officer is available to give effect to the statute."); *Maxwell v. Civil
26 Service Commission of Tucson*, 146 Ariz. 524, 526 (App. 1985)(citing Martin); *Rouse v. Scottsdale
27 Unified School District No. 48*, 156 Ariz. 369, 371 (App. 1987)(elected officials have same or even
28 higher level of presumption); *Havasupai Heights*, 167 Ariz. at 387 (Land Commissioner); *Elia v.
Arizona State Board of Dental Examiners*, 168 Ariz. 221, 229 (App. 1990); *Berenter v. Gallinger*,
173 Ariz. 75, 82 (App. 1992)(Department of Insurance hearing officer); *Lanthrop v. Arizona Board
of Chiropractic Examiners*, 182 Ariz. 172, 180 (App. 1995); *Shelby School v. Arizona State Board of
Education*, 192 Ariz. 156, 169 at ¶ 63 (App. 1998)(presumption applies despite investigation of
religion of applicant); *Pavlik v. Chinle Unified School District No. 24*, 985 P.2d 633, 639 at ¶ 24 (to
be published at 195 Ariz. 148)(App. 1999)(school board).


⁴⁶ 2 Davis and Pierce, Administrative Law Treatise (3rd ed. 1994)(hereinafter "D&P") § 9.8 at 68.

1 None of these types of bias are reflected in the record herein. In Arizona, bias may be shown
2 by an "irrevocably closed mind" or by "prejudgment of the specific facts that are at issue".⁴⁷ It is
3 clear from the record in this proceeding that any claims of bias against the Staff and the ALJ do not
4 demonstrate irrevocably closed minds or prejudgment of the facts at issue herein. Moreover, the
5 proceedings were conducted in a fair and impartial manner. The intervenors' allegations should
6 therefore be disregarded.

7 **VII. CONCLUSION**

8 In light of the reasons set forth above, and those discussed in Staff's initial closing brief,
9 Staff's recommendations should be adopted in this case.

10 RESPECTFULLY SUBMITTED this 21st day of March, 2014.

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13 
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35 ⁴⁷ *Havasu Heights*, 167 Ariz. at 387.

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